

Message Text

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ACTION EUR-25

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SUBJ: MALTA POUND EXCHANGE RATE CHANGES

REF: 10 FM 242

1. SUMMARY. THE RECENT INTERNATIONAL MONETARY CRISIS HAS HELPED TO BREAK THE TRADITIONAL MALTA POUND PARITY WITH THE POUND STERLING AND FORCES THE GOM TO INTRODUCE AN INDEPENDENT EXCHANGE RATE POLICY. THE PREMIUM OF THE MALTA POUND OVER STERLING REACHED A PEAK OF NEARLY 14 PERCENT ON JULY 9. END SUMMARY.

2. MALTA BROKE PARITY WITH STERLING IN AUGUST 1971 IN THE WAKE OF THE DOLLAR CRISIS. THE CENTRAL BANK OF MALTA ACT WAS AMENDED AT THAT TIME TO ALLOW THE CENTRAL BANK'S SPOT QUOTATIONS TO GO BEYOND THE PREVIOUS STATUTORY LIMIT OF 1 PERCENT EITHER SIDE OF PARITY WITH STERLING. ON AUGUST 25, 1971 THE MALTA POUND STOOD AT A 5 PERCENT PREMIUM OVER STERLING. ON SEPTEMBER 11, THE PREMIUM WAS REDUCED TO 2.5 PERCENT WHERE IT REMAINED UNTIL THE FLOTATION OF STERLING IN JUNE 1972.

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3. FACED WITH THE BRITISH GOVERNMENT'S DECISION ON

JUNE 23 TO FLOAT STERLING, THE GOM SUSPENDED FOREIGN EXCHANGES TRANSACTIONS FOR A FEW DAYS AND DECIDED TO INTRODUCE A NEW POLICY BY WHICH THE MALTA POUND/STERLING RATE OF EXCHANGE WOULD BE AT A LEVEL BETWEEN THAT OF STERLING AND THAT OF THE CURRENCIES OF MALTA'S MAJOR EUROPEAN TRADING PARTNERS. ON THE RESUMPTION OF BUSINESS ON JULY 1, 1972, THE SPOT RATE FOR THE MALTA POUND WORKED OUT AT A 5.5 PERCENT PREMIUM OVER STERLING. FROM THIS POINT IN TIME CHANGES IN OTHER CURRENCIES BEGAN TO HAVE MORE IMPORTANT REPERCUSSIONS ON THE MALTA POUND THAN CHANGES IN THE POUND STERLING ITSELF. EXPERIENCE HAS SHOWN THAT THE ITALIAN LIRA HAS BECOME ONE OF THE MOST IMPORTANT DETERMINANTS OF THE MALTA POUND RATE.

4. A RENEWED WEAKING OF STERLING TOWARDS THE LAST QUARTER OF 1972 TENDED TO PRODUCE A HIGHER MALTA POUND PREMIUM. IN THE LAST TWO MONTHS OF 1972 THE PREMIUM STABILIZED AT AROUND 7 PERCENT. THE MALTA POUND WAS ALSO AT A PREMIUM AGAINST THE US DOLLAR

AT THE END OF 1972, ON THE BASIS OF PARITIES RULING ON MAY 31, 1971. HOWEVER, MOST OF THE EUROPEAN CURRENCIES APPRECIATED EVEN MORE THAN THE MALTA POUND. CONSEQUENTLY, THE MALTA POUND WAS 2.1 PERCENT BELOW THE ITALIAN LIRA AT THE LOWER END AND 9.4 PERCENT BELOW THE SWISS FRANC AT THE HIGHER END. ON THE BASIS OF THE SMITHSONIAN PARITIES THE MALTA POUND WAS AT A PREMIUM ONLY OVER STERLING.

5. FROM A HIGH POINT OF 9.75 PERCENT IN MARCH 20, THE MALTA POUND PREMIUM OVER STERLING MOVED GRADUALLY DOWNWARDS, REACHING

A 6.625 PERCENT LEVEL BY MAY 18. IN THE FOLLOWING WEEKS, ALL THE MAJOR CURRENCIES, INCLUDING THE ITALIAN LIRA, STRENGTHENED FURTHER RELATIVE TO THE DOLLAR. THUS, ALTHOUGH STERLING REMAINED FIRM AGAINST THE DOLLAR, THE MALTA POUND PREMIUM OVER IT MOVED UP REACHING 7.5 PERCENT BY THE END OF MAY AND TOUCHING 8.875 PERCENT ON JUNE 5. SUBSEQUENTLY, AFTER STABILIZING AT AN AVERAGE LEVEL OF 7.5 PERCENT DURING THE SECOND WEEK IN JUNE, THE MALTA POUND PREMIUM REACHED A RECORD LEVEL OF NEARLY 14 PERCENT ON JULY 9.

6. COMMENT: AN IMPORTANT CONSIDERATION FOR GOM FINANCIAL AUTHORITIES
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IN ABSORbing THE VALUE OF THE MALTA POUND MORE ON CHANGES IN THE VALUE OF THE ITALIAN LIRA AND THE GERMAN MARKS HAS BEEN A GRADUAL SHIFT IN THE COUNTRY'S TRADE PATTERN AWAY FROM THE U.K. AND TOWARD THESE AND OTHER CONTINENTAL EUROPEAN COUNTRIES IN OTHER WORDS, THIS HAS BEEN ONE OF THE GOM'S TACTICS FOR WARDING OFF IMPORTED INFLATION.
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